## US Families and Intuitions: Financial Planning in the UK & Europe

Over the last few years, the number of Americans living in the UK, Europe and Israel has grown. Whether it be work, retirement, or realising a lifelong dream to live on the Côte d'Azur, Americans are moving in greater and greater numbers. What many don't realise though is that even if your location changes, your ties to the American tax system will remain. The citizenship-based system implemented by the US, has led to many 'accidental Americans'; those who never intended to be, but are within the US taxation system.

Whether the initial move was for a short-term secondment or a longer-term relocation, US families are impacted by the unique tax and compliance requirements set out by US law. For these families, wealth management isn't as simple as just managing an investment portfolio. They must consider a wide range of planning solutions to avoid the common pitfalls. Whilst there is no one-size-fits-all approach, there are some common factors that any US-connected family living in or moving to Europe should consider:

1. Strategic Financial Planning
2. Tax Treaties – Planning and Reporting
3. Currency Management
4. Estate Planning

### Strategic Financial Planning

There has been a raft of legislative changes around the world that have increased financial transparency between countries (CRS – Global, FATCA – US, IFI – France, Offshore Fund – UK). It is more important than ever that High Net Worth families have a clear financial plan, considering their total assets across jurisdictions.

To start with, families must review all of the different investment structures they hold internationally. On the face of it, individual accounts may be performing well from an investment perspective, but without considering the different tax regimes linked to the accounts, any gains could be completely eroded. There are numerous examples where savings accounts offer tax benefits for nationals, but are far from beneficial for US-linked families. In most instances, the US only recognises US-based plans, and products like ISAs in the UK and Assurance Vies in France typically do not qualify for US tax deferment. In some cases, these can still be used as part of an overall strategy, but families must be cautious about how they are invested and how they are utilised as part of the global management of the family's affairs.

Having a clear understanding of the family's long-term plans, and building this around their international accounts, means that families can then start to set out a long-term strategy, factoring in short-term cash-flow, saving for retirement, and succession planning. This can be difficult for international clients, as there are many items to consider. Families often struggle to identify their needs and requirements and end up having either solely US accounts (using an historic US address) and therefore being exposed to currency fluctuations, or having European accounts mismanaged from a US standpoint. Neither of these solutions are optimal for the long-term. These families who do not have their finances managed in a co-ordinated manner can often find themselves with too much exposure to an asset class, an individual security, or excessive levels of cash across their investment accounts.

A family's international finances should be managed as a single estate, utilising the international tax-friendly accounts as effectively as possible. e.g. a (401(k) and IRA in the US, SIPP accounts in the UK, 'Plan d'épargne en actions' in France and a 'Savings Plan for Every Child' in Israel. Using the tax-exempt accounts to hold high income-producing assets is one way of creating an effective strategy, ensuring that you avoid investing in foreign mutual funds is another. These funds are seen in the US as a Passive Foreign Investment Company (PFIC) and are to be avoided by US citizens. PFICs are subject to highly punitive tax treatment, incurring a higher tax rate than a similar US-listed fund and also involving additional reporting requirements, which can often be time-consuming and costly.

## Tax Treaties – Planning and Reporting

The US has tax treaties in place with over 65 countries globally. These treaties allow US citizens residing in foreign countries to be taxed at a reduced rate, or to be exempt from US taxes on certain items of income they receive from US sources. As part of the agreement, certain countries will not require tax to be paid on US sources of income. Each country has a different arrangement in place and some US states have their own individual set of rules, so it is important that families fully understand the relevant tax treaties when building their investment plans.

Different tax treaties offer a range of planning opportunities that families can make use of. Examples include the Franco-American tax treaty, whereby Americans living in France and investing in US assets are taxed in the US but are not required to pay the additional French tax of 17.2% CSG/CRDS.

Whilst local tax considerations must be considered, Americans planning on moving overseas must also consider their state of domicile within the US. If they elect a state where there is no income tax due, it will mean the family no longer has an obligation to pay state taxes as well as federal.

Many US citizens still use their US CPA to help with their planning and reporting. This can lead to issues. The lack of familiarity with global tax matters can lead to more tax being owed or having to reorganise their affairs at a later date, to become compliant. From a planning perspective, families with advisers who understand cross border issues can look to utilise items such as foreign tax credits, making tax-efficient charitable donations and pension contributions, ensuring they are timed correctly to coincide with both the US and local tax year.

Any investments, in the US or in France, UK, Italy or Israel, will need to be fully reported to the US in USD on a calendar year basis, in addition to reporting them in the local currency of the country the family are residing in. US reporting requirements include providing details of all sources of income, gains and losses – something many domestic managers do not have the capability to do. This doesn't mean that all assets must be based in the US, but it does mean that any investments must be made considering USD gains and losses, long-term versus short-term gains and how much income has been generated. Having advisers and investment managers who can review and report on all the estate in USD and domestic currency means that it is possible to minimise the gains in both USD and the local currency. In addition, providing a simple 1099 in USD on the European portfolios will put you in the good books of your US CPA, as they no longer have to go line by line through a statement, translating all the figures into USD.

## Currency Management

Managing currency is often one of the final things considered by international families. Some leave their assets in the US with existing managers, which may be suitable if the family plan on moving back to the US in the short term. However, for families who plan on remaining outside the US for the long term, or for an undecided period, this can result in exposure to unnecessary exchange rate risk. If the dollar weakened, it would leave them with a significant shortfall in income if all their cash requirements are in Sterling, Euro or Israeli Shekel.

The basic purpose of an investment portfolio is for the value to grow over time. However, these returns can be nullified if there are significant movements in exchange rates over the same period. For example, if the Dollar moved by 3% versus the Euro in a given year and 4.5% against the Pound, in a low growth environment these swings can significantly impact the returns of the portfolio. With this in mind, it is important to build a long-term plan considering three separate buckets: short, medium and long-term requirements.

Whether it's short-term cash for daily expenditure, or long-term retirement planning, currency needs to be considered and budgeted for. Having the ability to match your liabilities without the added concern of a shift in exchange rate is important.

An investment manager working with an international family must be able to build a portfolio which takes currency movement and reporting into account. The manager needs to review the portfolios in dollar and the local currency, matching losses versus gains and therefore effectively managing the accounts in both jurisdictions.

A parallel issue is opening a bank account as an American citizen. Many US institutions will no longer work with Americans living overseas, and likewise many European banks will not work with US citizens. It is important for families to be able to have access to a full suite of services, including debit/chequebook facilities, minimal costs on transferring money from one currency to another, or to a local bank and the option of margin loans against the portfolios. Due to the limited number of companies that are able to work with Americans, clients often stumble across a solution that provides an element of the full service and try to make do. This inevitably unravels further down the line, especially when using a parent's address on brokerage accounts, which can lead to portfolios being suspended or closed.

## Estate Planning

Similar to tax and reporting, each country has a different set of rules and paying close attention to these changes is crucial.

As with any international family, estate planning needs to be kept up-to-date. Many families are often unaware that any estate planning that has been done in the US prior to departure, is often disregarded by authorities in their new location. This approach typically leads to problems down the road and results in costly work to reorganise the estate.

Changes brought in by the 2015 European Union Succession Regulation have allowed individuals to opt out of 'forced heirship' rules that are applied in some EU countries. This is a significant issue; if a US Will has not been updated accordingly and a family member passes away, their assets can still be considered under the original rules, leading to complications in the succession plan.

Similarly, the way a pre-existing Trust is treated can differ whilst living overseas. Trusts are a very common aspect of US planning. In countries where the forced heirship rules apply, the utilisation of a Trust can appear to go against these rules and their legitimacy can be challenged.

With each country applying different rules, suitable estate planning requires intricate knowledge of the relevant structures and circumstances, including the underlying investments. Otherwise, families can get penalised by an increase in tax both in the local jurisdiction and in the US.

## Summary

Managing a regular investment portfolio or family estate is complicated by any means. Moving to another country with new laws and regulations written in a foreign language, creates even more complexity. Appointing an international wealth manager with an intricate knowledge of local requirements can be the key to successful financial planning, leaving you free to enjoy your new life abroad.

This article covers some of the key considerations to be aware of. As every family has a range of circumstances that need to be analysed and considered, we encourage you to contact us to see how we can help you and your family: info@civilsaint.com

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